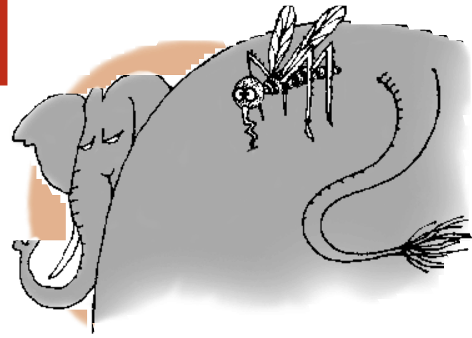
Micro Law



US v. *Microsoft* (again) – The browser war

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Bill Gates has a Win 95 contract with Compaq for preloading Win 95 on Compaq PCs. The contract requires Compaq to preload Win 95 in the same form (without modification) in which Microsoft provides Win 95. That form includes Internet Explorer 3 (IE 3) as a component of the total software package. (This is something like the way Sun licensed Java to Microsoft, although not the way Microsoft distributed its version. Hence, the *Sun* v. *Microsoft* suit.) Compaq wanted to ship some of its PCs with Netscape instead of IE, or at least to replace the IE 3 icon on the PC's Win 95 start-up screen with a Netscape icon. Microsoft told Compaq that if it did so, Microsoft would terminate Compaq's Win 95 license. Compaq backed down. (See the Compaq box.)

The graphic that you are seeing, at the upper right, is more conceptual than narrative. It shows a gnat biting the backside of an elephant. That is a personal metaphor from my days in the 1970s as chief of the DOJ Antitrust Division's patent section. The graphic symbolizes the gap between reality and antitrust enforcement officials' self-perceptions. The gnat (a US antitrust prosecutor—then or now) is telling himself, "Boy, am I about to stampede that elephant." The elephant remains oblivious and follows Newton's first law (or a special case of Newton's second law, $F = ma$, in which $a \approx 0$ because $m >> F$.) This graphic raises the question of what long-term effect the present DOJ case against Microsoft will have on Microsoft and the computer industry.

What's going on here?

To refresh your recollection, see the box on p. 4 for a recapitulation of what CNET has termed "Microsoft's antitrust trail of tears." The current posture of the saga of the gnat biting Microsoft's buttock is that the DOJ has charged Microsoft with violating the 1996 wrist-slap decree by, among other things, strong-arming Compaq. The government has asked the court to hold Microsoft in contempt of court. Microsoft is restraining itself as the DOJ asks it, "Are you trying to show your contempt for this decree?" from replying, "No, sir, I'm trying to conceal it."

The critical question in this contempt proceeding is *not* whether Microsoft is violating the antitrust laws by what it is doing with IE and Win 95. The only issue is whether the 1995 consent judgment (consent decree) forbids what Microsoft is doing. A consent judgment is like a contract. The defendant promises to do what the judgment provides, to settle the case. Whether the antitrust laws say the same thing as the consent judgment is beside the point. The consent judgment may say more or say less than what the antitrust laws require.

Thus, a consent judgment may prohibit acts that do not violate the antitrust laws. This would be based on the theory that the defendant needs some "fencing in" to give competition some breathing room against this defendant, and to keep it from "exploring as yet untraveled roads" to wreak similar competitive havoc. Ordinarily, a consent decree is fairly specific, and it does not even try to forbid the defendant from doing things that were not the subject of the case that led to the decree. A decree against tie-ins ordinarily won't prohibit price-fixing. The bottom line is that if a given antitrust violation is not covered by the undertakings in the consent judgment, the government must bring a new lawsuit to curb that practice. That may be the case here.

The critical passage in this consent judgment is section IV(E), which provides:

> E. Microsoft shall not enter into any License Agreement [with an OEM] in which the terms of that agreement are expressly or impliedly

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The Compaq episode

In 1996 Compaq took the IE 3 icon off the Win 95 Start menu of Compaq's Presario PCs because Compaq had formed a browser "partnership" with Netscape. They wanted to place a Netscape icon on the Start menu instead.

The significance of an icon's being on the screen is that a user brings up the application (IE browser or Netscape browser, as the case may be) just by clicking on the icon. Otherwise, the user must click on Win 95's START button on the screen's bottom toolbar; move the cursor up to Programs; pause and move the cursor right and then up or down to the application's family name (file folder), for example, Netscape Navigator Gold 3; pause and then move the cursor to the Netscape browser icon. (This is why informed users learn how to create shortcut icons for applications that they frequently use.)

On May 30, 1996, Microsoft sent Compaq a letter advising it that Microsoft was terminating Compaq's Win 95 license. The following is an excerpt from the deposition transcript of Compaq's director of software procurement Stephen Decker, whom the government subpoenaed to testify during its investigation of Microsoft:

> Q. How did Microsoft respond to Compaq removing the Internet Explorer icon from the desktop?
>
> A. Well, when they found out about it, they sent a letter to us telling us that, you know, they would terminate our agreement for doing so.
>
> Q. [Why did they do that?]
>
> A. Well, I believe that the reason for Microsoft wanting that was because the icon represents the ease of use for the customer. Therefore, with the icon of the Internet Explorer visible and available to the consumer, they would naturally migrate to that particular product versus any other product that would be in a file folder.
>
> Q. After Compaq received the letter from Microsoft threatening to terminate the license agreement, what did Compaq do?
>
> A. We went back and reworked the code so that we put an [IE 3] icon back on.

Microsoft and Compaq conferred (meaning Compaq groveled and pleaded for mercy), and Microsoft then sent Compaq this letter:

> June 6, 1996
> Ms. Celeste Dunn, Vice President
> Consumer Software Business Unit, Compaq
> Re: Notice of Intent to Terminate License Agreement
> Dear Celeste:
>
> I appreciated speaking with you over the phone earlier today. As we discussed, in the spirit of reinstating mutual cooperation and trust, we would like to resolve the above mentioned Notice of Intent to Terminate letter in as quick and mutually agreeable manner as possible.
>
> To accomplish this, Microsoft is requesting that Compaq replace the Microsoft Network and Internet Explorer icons on the Windows 95 desktop on all Compaq Presario machines. Specifically we are asking that these icons be put back on the Windows 95 desktop so they look and function exactly the same as how they were originally provided by Microsoft and/or Authorized Replicators. This means the icons should not be just Windows 95 shortcuts, since the functionality is different. In addition, the Microsoft Network and Internet Explorer icons and Internet Setup Wizard icon should also be put back into their original locations and functionality under the "Start" button on Windows 95.
>
> If you are willing to give Microsoft a clear written assurance that the above will be implemented on all Compaq Presario machines within sixty (60) days of the date of this letter, Microsoft will withdraw its Notice of Intent to Terminate letter.
>
> Once again, we appreciate your openness and willingness to discuss and resolve the above issues.
> Sincerely,
> Don Hardwick, Group Manager, OEM Sales Division

In his deposition Decker was asked whether Compaq was considering Netscape as an alternative for IE 4:

> A. Not that I'm aware of.
>
> Q. Why has Compaq not considered Netcaster today as an alternative to Internet Explorer 4.0?
>
> A. I would say the major reason Compaq hasn't is because the category of browser is now fulfilled with the Internet Explorer product which will be a part of the Microsoft operating system. Therefore, Compaq will get this as part of the operating system code and that category will be filled. So therefore we would not have to go out and negotiate something separately and potentially pay some fees, and also take up additional real estate on our hard drive.

conditioned upon:

> (i) the licensing of any other Covered Product, Operating system Software product or other product (provided, however, that this provision in and of itself shall not be construed to prohibit Microsoft from developing integrated products); or
>
> (ii) the OEM not licensing, purchasing, using or distributing any non-Microsoft product.

The DOJ petition contends that Microsoft violated clause (i) by expressly conditioning the licensing of Win 95 upon a tie with IE 3 or IE 4. In response, Microsoft contends that the parenthetical part of clause (i) expressly allows it to integrate IE with Win 95, which it has done. Microsoft admits that it told Compaq and other PC manufacturers that it would terminate their Win 95 licenses if they took the IE icon off the Start menu. But Microsoft maintains that this is no different than a

The government's tilt against Gates' windmill

After years of rumblings from the computer software industry, in 1989 the Federal Trade Commission finally started investigating whether Microsoft's MS-DOS licensing practices were curbing competition. In 1993, the FTC Commissioners tied 2-2, on two occasions several months apart, on whether to do anything. The FTC then closed its investigation.

The DOJ's Antitrust Division then began its own investigation of Microsoft. In July 1994, the DOJ and Microsoft announced a negotiated settlement. They agreed to a consent decree, slapping Microsoft on the wrist, prohibiting "per-box" or "per-processor" licensing, and ignoring vaporware issues.

In February 1995, DC Judge Stanley Sporkin rejected the MS-DOJ settlement as inadequate. (He said that the DOJ and Microsoft were stonewalling him on the facts and treating him like a mushroom by placing him in a dark corner of a cellar and sprinkling him with fertilizer. (See Micro Law, Apr. 1995, pp. 6-7.) Microsoft and the DOJ appealed, and in June 1995 the DC Court of Appeals reversed, taking Sporkin off the case and reassigning it to Judge Thomas Jackson, who promptly approved the consent decree (Aug. 1995). Meanwhile the DOJ began to investigate bundling of IE with Win 95.

In July 1996, Caldera (a successor to the interests in DR-DOS) sued Microsoft for antitrust violations for the kind of conduct alleged in the now-settled DOJ case against Microsoft. In August of 1996, Netscape complained to the DOJ that Microsoft was resuming its anticompetitive practices by forcing IE on PC manufacturers as part of a campaign to squelch Netscape. The DOJ opened a new investigation.

In February 1997, Texas' attorney general launched an antitrust probe of Microsoft. Several senators then asked the FTC to investigate Microsoft's compliance with the 1995 consent judgment, but in July 1997 the FTC refused. California, Connecticut, Massachusetts, and New York joined Texas in probing Microsoft's methods of persuading PC OEMs to use IE but not other browsers. In October 1997, Ralph Nader announced a Nov. 1997 conference to study Microsoft's alleged monopolistic practices. Rumors of a parallel European Union investigation circulate.

The DOJ continued to investigate Microsoft. October 20, 1997, the DOJ filed a contempt petition in federal district court in the District of Columbia. The petition asserts that Microsoft is committing contempt of court by violating the consent decree, that is, by tying IE3 and IE4 with Win 95. The government asked the court to order Microsoft to comply with the consent decree and to impose a fine of $1 million per day on Microsoft if it does not immediately comply with the court's order. The Antitrust Division indicates that it is continuing a broader investigation of Microsoft's practices.

In November 1997, Senator Hatch (R-UT), Senate Judiciary Committee chair, held a hearing to examine Microsoft's Internet-related practices. Hatch states, "No one company should be able to dominate everything in one industry."

Also in November, Texas sued Microsoft in state court, alleging that Microsoft contracts with OEMs are illegal because they interfere with the state's Microsoft antitrust investigation. The contracts bar OEMs from disclosing information about Microsoft without its prior approval. "Manufacturers are afraid to come forward with information," said Texas' attorney general. Microsoft denies this, saying that OEMs are not afraid to provide information simply because they must first advise Microsoft that they are doing so. Hatch says that he thinks the "don't tell without asking" agreements are illegal.

landlord telling a tenant that he'll be evicted when he says he won't pay the rent in accordance with his lease.

(Neither party has said a word about clause (ii). Also, there appears to be no controversy over the fact that Microsoft charges licensees nothing extra for IE. The DOJ apparently buys Microsoft's story that this is no different from giving a toy whistle away with a box of CrackerJacks. Moreover, anyone can download both Netscape and IE free of charge from Web sites.)

IMHO, as we say on the Net; they're both barking up the wrong tree. First, clause IV(E)(i) of the consent judgment is a fiasco, or at least highly problematic, as far as this kind of bullying is concerned. Does it even touch what Microsoft did? I don't think so. This part of the judgment says that Microsoft must not *condition* a Win 95 *license* on the OEM's also *licensing* IE. To condition a license means to require an unwilling licensee to buy or accept an additional license that it does not want. That is not what happened here. Compaq willingly took both a Win 95 license and an IE license. It uses, and wants to use, the Win 95 license with all of its PCs, since it is commercially impracticable to market a PC without preloading Win 95 on it. Compaq uses and wants to use the IE license with some of its PCs or maybe all of them. Compaq just didn't want to have the IE icon pop up on the start-up screen, and maybe Compaq didn't want even to preload IE in some Compaq PCs. In short, Microsoft didn't make Compaq take an IE license it didn't want. The dispute is over the extent to which (or how) Compaq will use its rights under the IE license and will distribute IE to Compaq's end users. Clause IV(E)(i) doesn't say anything about that.

An alternative interpretation of what Microsoft did is that it required, as part of its standard Win 95 license, all licensees to use licensed object code—or perhaps a package containing a SETUP.EXE—exactly the way Microsoft delivered it, without any modification. This prevented nonloading or deletion of the icon or the IE code module from the code that Compaq loaded. That module apparently placed IE 3 on the highly conspicuous Start menu. This still doesn't look like a licensing tie, but instead just a use restriction (maybe an illegal one, but that's not the point) on what

licensees may do with the licensed code that Microsoft provides.

Either way, courts do not consider that it is their job to rewrite parties' contracts to say what they should have said. The exception to this, perhaps, is when one of the parties is a powerful bank or insurance company and the other party is a poor old widow lady at the firm's mercy. The DOJ could persuade a court that Microsoft is equivalent to the bank or insurance company of this parable. The DOJ will not likely succeed, however, in cloaking itself for court with the rags of the poor old widow lady.

On the other hand, the parenthetical phrase doesn't say what Microsoft claims. The parenthetical phrase says that clause IV(E)(i) does not, in and of itself, prohibit Microsoft from developing integrated products. It is unnecessary to decide whether IE is integrated with Win 95. (Probably, IE 3 is not and IE 4 may be, or if IE 4 isn't IE 5 surely will be.) It is unnecessary because clause (i)'s failure to prohibit Microsoft from *developing* an integrated product doesn't authorize Microsoft to force the resulting integrated product upon anybody who doesn't want it. As clause (i) is worded, Microsoft can develop all the integrated software products that it wants. But nothing in clause (i) says, "Go forth, Microsoft, and feel free to jam the entirety of the integrated products that you develop down every OEM's throat." Microsoft is as far off base (or farther) in its interpretation of the part of clause (i) inside the parentheses as the DOJ is about the part outside them.

Where does that leave us?

Why doesn't anybody say anything about clause (ii)? It's not even mentioned in the DOJ's contempt petition. Clause (ii) says that Microsoft shall not "expressly or impliedly condition" a Win 95 license on "the OEM not licensing, purchasing, using, or distributing any non-Microsoft product."

What's implied conditioning? A reasonable interpretation of this language is suggested by the judicial interpretation of section 3 of the Clayton Act. This is an antitrust law against exclusive dealing agreements, requirements contracts, and tie-in sales that may have the effect of lessening competition substantially. This section prohibits sales contracts made on the "condition, agreement, or understanding" that the customer won't use or deal in the goods of a seller's competitor. Consider a total requirements contract, an 80% requirements contract, or a large sale of a fixed amount of goods. The agreement may not, of itself, prohibit a customer from buying other goods from a seller's competitor. Nonetheless, that can be the agreement's effect. Consider also a software-hardware tie-in agreement. For example, I sell you a PC with a preloaded operating system (say, MS-DOS) on it. The tie-in sale may not in terms provide that you shall not buy somebody else's operating system software (say, DR-DOS). Nonetheless, that may be its practical effect. Accordingly, courts have interpreted section 3 of the Clayton Act to cover such agreements.

It is therefore reasonable to say that implied conditioning is something that is the necessary consequence of one's sales agreement practices. How does that apply to IE and section (ii)? Some of the files that IE puts on a disk are very large. For example, it may set aside 19 Mbytes for its mail storage. Some PCs (such as a laptop or your old 486) cannot support both IE and Netscape. For such a PC, installing IE may have the effect that there is no room for Netscape too. Perhaps that is not true for a new Compaq desktop with a hard disk drive that is 3 Gbytes or bigger. On the other hand, Compaq's software procurement director did testify that using up "additional real estate" on the hard disk was a reason why Compaq did not consider loading Netscape on Compaq PCs along with IE 4. The DOJ's failure even to mention clause (ii) is therefore curious.

In summary, section IV(E)(i) of the existing consent decree is probably a fiasco as far as forcing IE and its icon on PC manufacturers and their customers. While section IV(E)(ii) might possibly be interpreted to apply, the DOJ has forgotten about its existence or doesn't care, and Microsoft is not going to remind the gnat that it is biting the wrong buttock.

More generally, as long as Microsoft does not require PC manufacturers not to preload Netscape and not to put its icon on the screen along with IE, is there any competitive problem at all? Perhaps. The answer turns on a fact question: How much of a deterrent is it for enough end users to comprise a viable market for whatever Netscape is marketing to be faced with a screen on which IE 4 is an icon? Is it enough of an obstacle that Netscape or other browser wanna-bes are blocked from the market?

It's not a deterrent for me. I simply downloaded Netscape from its free Web site and created a shortcut browser icon. I have IE 3, which I don't like, off in a corner of the screen and haven't even got around to downloading and installing IE 4. For me, using Netscape instead of IE is not a marketing obstacle for Netscape to worry about. Most readers of *IEEE Micro* may think the same thing. But that bit of introspection isn't market research, and it is unrealistic to imagine that this account presents a valid picture of what Netscape's marketers are really up against. (They cannot make a living just dealing with members of the IEEE Computer Society.) I don't know the answer to the question posed. But I suspect that Gates does know, and I am willing to assume that he or Microsoft has good reason to throw a major fit when an OEM deletes the IE icon. If Microsoft says it's important, we should take Microsoft at its word.

If it is a real concern, however, the Antitrust Division may well need to bring a new antitrust case against Microsoft to cope with this practice. That raises several legal, factual, and policy issues. Is there really anything wrong (under the antitrust laws) with what Microsoft is doing? Can anything be imagined that would cope with what Microsoft is doing? Would the imagined course of action be practicable? To the extent that it means getting a court to act to restrain Microsoft, could the proposed intervention be supported by a legally sound theory under present law? Will the gnat succeed or end up getting trampled? Will there ever be solid answers? Tune in to the next *IEEE Micro* issue for the exciting conclusion (maybe) in Episode 2—"The Gnat versus the Borg!"